

Report of the auditor-general to the Free State Legislature and the council on the Mantsopa Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Mantsopa Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2017, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the effects of the matters described in the basis for qualified opinion section of my report, the financial statements present fairly, in all material respects, the financial position of the Mantsopa Local Municipality as at 30 June 2017, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2016 (Act No. 3 of 2016) (DoRA).

Basis for qualified opinion

Property, plant and equipment

3. The municipality did not recognise all items of land included in property, plant and equipment in accordance with GRAP 17 *Property, plant and equipment*. Restatements to the cost of land were incorrectly calculated. Consequently, property, plant and equipment was overstated by R63 204 380. Some of the items included in land were further incorrectly recognised as they should have been recognised as investment property. Consequently, property, plant and equipment was overstated and investment property understated by R136 787 696.
4. The municipality did not recognise all items of infrastructure included in property, plant and equipment in accordance with GRAP 17 *Property, plant and equipment*. Restatements to the cost of infrastructure were incorrectly calculated. Consequently, property, plant and equipment was overstated by R8 425 659. Additionally, there was a resultant impact on the accumulated surplus.

Investment property

5. I was unable to obtain sufficient appropriate audit evidence for the value of buildings included in investment property as the municipality did not maintain adequate supporting documentation for recorded values. Consequently, I was unable to determine whether any adjustment was necessary to investment property stated at R 112 448 145 (2016: R112 448 145) in note 9 to the financial statements.

Service charges

6. During 2016, the municipality did not recognise revenue from exchange transactions in accordance with GRAP 9, *Revenue from exchange transactions*. Service charges were incorrectly calculated and levied on consumer accounts, which resulted in revenue from service charges and consumer debtors being understated by R104 293 372. In addition, I was unable to obtain sufficient appropriate audit evidence that the municipality had properly charged and accounted for income from service charges, due to the status of the accounting records. I was unable to confirm revenue from service charges by alternative means. Consequently, I was unable to determine whether any adjustment to service charges stated at R93 725 750 in the financial statements, was necessary. My audit opinion on the financial statements for the period ended 30 June 2016 was modified accordingly. My opinion on the current period's financial statements was also modified because of the possible effect on this matter on the comparability of the current period's figures.

Inventory

7. The municipality recognised items that did not meet the definition of inventory in accordance with GRAP 12, *Inventory*. Properties held for sale in the ordinary course of business that had been disposed were still included in inventory. Consequently, inventory was overstated by R24 599 953. There was a resultant impact on the surplus for the period and on the accumulated surplus.

Context for the opinion

8. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of my report.
9. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
10. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Material uncertainty related to going concern

11. Note 46 in the financial statements indicates that the municipality incurred a net loss of R4 502 317 during the year ended 30 June 2017 and there has been a significant increase in accounts payable of R42 413 306 (2016: R25 914 603). In addition, the municipality owed Eskom R82 670 922 (2016: R63 777 928) as at 30 June 2017 which is long overdue. These conditions, along with other matters as set forth in note 46, indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern and to meet its service delivery objectives.

Emphasis of matters

12. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unauthorised expenditure

13. As disclosed in note 47 to the financial statements, the municipality incurred unauthorised expenditure of R98 576 284 (2016: R36 493 000) during the year due to expenditure that exceeded the limits provided for in the main divisions of the approved budget.

Irregular expenditure

14. As disclosed in note 49 to the financial statements, the municipality incurred irregular expenditure of R7 344 653 (2016: R23 791 583) during the year due to non-compliance with supply chain management requirements. In addition, the full extent of irregular expenditure during the year was still in the process of being determined.

Fruitless and wasteful expenditure

15. As disclosed in note 48 to the financial statements, the municipality incurred fruitless and wasteful expenditure of R14 239 064 (2016: R9 986 761) during the year due to interest and penalty charges on the late payment of suppliers

Restatement of corresponding figures

16. As disclosed in notes 43 to the financial statements, the corresponding figures for 30 June 2016 have been restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2017.

Material losses

17. As disclosed in note 54 to the financial statements, water distribution losses of R1 724 285 (2016: R1 104 573) and electricity distribution losses of R13 973 066 (2016: R11 805 174) were incurred by the municipality mainly due to leakages, illegal connections, burst water pipes, line losses, tampering and theft.

Material impairments

18. As disclosed in note 7 to the financial statements, receivables from exchange and non-exchange transactions were impaired by R167 607 378 (2016: R177 565 081).

Other matters

19. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited disclosure notes

20. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure

requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion on it.

Responsibilities of the accounting officer for the financial statements

21. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
22. In preparing the financial statements, the accounting officer is responsible for assessing the Mantsopa Local Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the intention is to liquidate the municipality or to cease operations, or there is no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

23. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
24. A further description of my responsibilities for the audit of the financial statements is included in the annexure to the auditor's report.

Report on the audit of the annual performance report

Introduction and scope

25. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected key performance areas (KPA's) presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
26. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.

27. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected KPAs presented in the annual performance report of the municipality for the year ended 30 June 2017:

KPA	Pages in the annual performance report
KPA 2 – Basic Services- community development and social cohesion	xx – xx

28. I performed procedures to determine whether the reported performance information was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
29. The material findings in respect of the usefulness and reliability of the selected KPA are as follows:

KPA 2 – basic service-community development and social cohesion

Various indicators

30. Planned indicators and targets included in the service delivery and budget implementation plan (SDBIP) were not consistent with reported indicators and targets as the indicators below were not included in the annual performance report (APR). This is not in line with the requirements of section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000)

Indicator	Planned target
Reduce water loss in distribution by 40% through installation of bulk meters	40%
Achieve 90% compliance with green drop waste water quality accreditation system	90%
Annual inspection of 1993 electricity meters	1993
Annually review the integrated environmental plan	Annual review of the current Integrated Environmental Management Plan
Promulgate waste management and waste collection by laws	2 waste related bylaws promulgated
Divert 15 000 kg of recyclable waste from the landfill site to the Buy-back centre	15 000 kg

31. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the indicators listed below. This was due to the unavailability of supporting documentation. I was unable to confirm the reported achievement by alternative means.

Indicator	Reported achievement
Infrastructure - Patching of potholes on 4kms damaged tarred roads/streets in all towns	2,675 km
Infrastructure - Re-gravel 2km of streets/roads in Ladybrand / Manyatseng	350m
Infrastructure - Reshaping (Grading) of 2km streets in Ladybrand and Manyatseng	2,23km
Infrastructure - Regravel of 1km of streets/roads in Excelsior / Mahlatswetsa	50m
Electricity - Maintain at least 5 substations annually	5
Electricity - Maintain 2185 street lights in accordance with maintenance program	90

32. The target achievement reported for the indicators below were misstated when compared to evidence provided.

Indicator	Reported achievement	Audited achievement
Infrastructure - Maintain 5km of Storm water channels	5,060 km	3, 070km
Infrastructure - Construct 1,6km new storm water	0,6km	1,2km
Water - Provide 383 households with potable water supply using communal water tankers to occupied erven of 383 without standpipes at Manyatseng ext.9 and 8 farming villages	383	325

33. The systems and processes to enable reliable reporting of the actual service delivery against the indicators were not adequately designed and implemented as required by the FMPPPI. As a result, I was unable to obtain sufficient appropriate audit evidence to support the reported achievements of the indicators listed below due to these limitations placed on the scope of my work. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements of these indicators.

Indicator	Reported achievement
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Continuously provide 15 170 households with access to basic water supplies within RDP standards	15 170
Refuse - Weekly collection of refuse in all 15 170 households	15 170
Continuously provide 15 553 households with access to basic sanitation services.	15 553
Continuously provide 15170 Households on formalised erven with access to electricity services	15 170

Other matters

34. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Achievement of planned targets

35. Refer to the annual performance report on pages x to x; x to x for information on the achievement of planned targets for the year and explanations provided for the underachievement of a significant number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 30 to 34 of this report.

Report on the audit of compliance with legislation

Introduction and scope

36. In accordance with the PAA and the general notice issued in terms thereof I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
37. The material findings in respect of the compliance criteria for the applicable subject matters are as follows:

Budget

38. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R98 576 284, as disclosed in note 47 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by inadequate budgeting for non-cash items included in expenditure. Unauthorised expenditure amounting to R51 684 974 was incurred on depreciation.

Annual financial statements

39. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently

corrected, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

Strategic planning and performance management

40. A performance management system was not established or adopted as required by section 38(a) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and municipal planning and performance management regulation 8.

Expenditure management

41. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
42. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, as required by section 65(2)(b) of the MFMA.
43. Effective steps were not taken to prevent irregular expenditure amounting to R7 344 653 as disclosed in note 49 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by not implementing adequate procedures and processes to ensure compliance with SCM regulations.
44. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R14 239 064, as disclosed in note 48 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest on overdue accounts to suppliers.

Revenue management

45. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
46. I could not obtain sufficient audit evidence that interest had been charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

Asset management

47. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
48. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.

Liability management

49. An effective system of internal control for liabilities including a liability register was not in place, as required by section 63(2)(c) of the MFMA.
50. An adequate management, accounting and information system which accounts for liabilities was not in place, as required by section 63(2)(a) of the MFMA.

Conditional grants

51. The municipality did not evaluate its performance in respect of programmes funded by the Municipal Infrastructure Grant, as required by section 12(5) of the DoRA.

Consequence management

52. Authorisation of unauthorised expenditure amounting to R98 576 284 was not done through an adjustment budget, as required by section 32(2)(a)(i) of the MFMA.

Human resource management

53. Appropriate systems and procedures to monitor, measure and evaluate performance of staff were not developed and adopted as required by section 67(1)(d) of the MSA

Procurement and contract management

54. Sufficient appropriate audit evidence could not be obtained that goods and services with a transaction value of below R200 000 were procured using price quotations as required by SCM regulation 17(a) and (c). Similar non-compliance was also reported in the prior year.
55. Quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c). Similar non-compliance was also reported in the prior year.
56. Competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2).
57. The preference point system was not applied in procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act, 2000 (Act No.5 of 2000) (PPPFA) and Treasury Regulations 16A6.3(b). Similar non-compliance was also reported in the prior year.
58. Bid documentation for procurement of commodities designated for local content and production, did not stipulate the minimum threshold for local production and content as required by Preferential Procurement Regulation (PPR) 9(1).
59. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA. Similar non-compliance was also reported in the prior year.
60. Awards were made to providers who were in the service of other state institutions or whose directors / principal shareholders were in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulation 44.

Other information

61. The Mantsopa Local Municipality's accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report

thereon and those selected KPAs presented in the annual performance report that have been specifically reported on in the auditor's report.

62. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
63. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected KPAs presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
64. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected I may have to re-issue my auditor's report amended as appropriate, however, if it is corrected this will not be necessary.

Internal control deficiencies

65. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.
66. Leadership did not provide sufficient oversight over financial and performance reporting and compliance and related internal controls, as material repeat findings were identified in the current year.
67. Leadership did not implement adequate and effective monitoring controls over the implementation of actions to address prior year reported matters. This has resulted in repeat findings that have not been addressed.
68. Leadership did not take effective steps to ensure that there were consequences for poor performance and transgressions, as no official was held responsible for the unauthorised, irregular, and fruitless and wasteful expenditure incurred by the municipality.
69. Management did not maintain proper record keeping to support performance reporting. Performance reports were not always supported by adequate records which resulted in significant findings being reported. This was due to the lack of competencies and inadequate training for senior and operational staff on performance planning, monitoring and reporting.
70. Management did not prioritise the review and monitoring of compliance with legislation, which resulted in repeat findings being reported. This was due to lack of consequence management as officials were not held accountable for non- compliance.

71. Management did not implement adequate review and supervisory controls over financial and performance reporting so that errors could be timely identified and corrected resulting in significant repeat findings that could have been prevented.
72. Management did not adequately implement risk management strategies to prevent/mitigate risks relating to financial and performance reporting as risks to financial and performance reporting were not timely detected and or prevented. This is mainly due to inadequate implementation of risk strategies by management.

Auditor - General

Bloemfontein

30 November 2017



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general's responsibility for the audit

As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected key performance areas and on the municipality's compliance with respect to the selected subject matters.

Financial statements

73. In addition to my responsibility for the audit of the financial statements as described in the auditor's report, I also:

- identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control.
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
- conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Mantsopa Local Municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor's report. However, future events or conditions may cause a municipality to cease to continue as a going concern.
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Communication with those charged with governance

74. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

75. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other

matters that may reasonably be thought to have a bearing on my independence and here applicable, related safeguards.